Q4 2022 Tapestry Inc Earnings Call - Final

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Presentation

OPERATOR: Good day, and welcome to this Tapestry conference call. Today's call is being recorded. (Operator Instructions)

Please note, this call may be recorded. At this time, for opening remarks and introductions, I would like to turn the call over to the Global Head of Investor Relations, Christina Colone.

CHRISTINA COLONE, GLOBAL HEAD OF IR, TAPESTRY, INC.: Good morning. Thank you for joining us. With me today to discuss our fourth quarter and year-end results, as well as our strategies and outlook, are Joanne Crevoiserat, Tapestry's Chief Executive Officer; and Scott Roe, Tapestry's Chief Financial Officer and Chief Operating Officer.

Before we begin, we must point out that this conference call will involve certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act. This includes projections for our business in the current or future quarters or fiscal years. Forward-looking statements are not guarantees, and our actual results may differ materially from those expressed or implied in the forward-looking statements. Please refer to our annual report on Form 10-K, the press release issued this morning and our other filings with the Securities and Exchange Commission for a complete list of risks and other important factors that could impact our future results and performance.

Non-GAAP financial measures are included in our comments today and in our presentation slides. Given that FY '21 included an additional week in the fourth quarter, the year referenced in today's comments will be on a comparable 13- and 52-week basis unless otherwise noted. For a full reconciliation to corresponding GAAP financial information, please visit our website, *www.tapestry.com/investors*, and then view the earnings release and the presentation posted today.

Now let me outline the speakers and topics for this conference call. Joanne will begin with highlights for Tapestry and our brands; Scott will continue with our financial results, capital allocation priorities and outlook going forward. Following that, we will hold a question-and-answer session, where we will be joined by Todd Kahn, CEO and Brand President of Coach. After Q&A, Joanne will conclude with brief closing remarks.

I'd now like to turn it over to Joanne Crevoiserat, Tapestry's CEO.

JOANNE C. CREVOISERAT, PRESIDENT, CEO & DIRECTOR, TAPESTRY, INC.: Good morning. Thank you, Christina, and welcome, everyone. We drove standout results this fiscal year, delivering accelerated revenue and profit growth across our portfolio, a direct reflection of the vibrancy of our brands and the agility and ingenuity of our talented teams around the world.

Our performance also demonstrates both our competitive advantages as well as the success of our strategic growth agenda, which we developed nearly 3 years ago to radically transform our organization to compete and win in a

new world of retail. This meant changing the way we worked, adopting a more consumer-centric mindset and utilizing our data-rich platform to acquire new consumers and better connect with our existing customers.

At the same time, our ambition required a commitment to leading in digital to complement our world-class store operations, recognizing the increasing importance of the omnichannel journey. We also embraced the need to fundamentally pivot, driving efficiencies in many areas of the business to support brand building and high-return investments.

Overall, we had to be more agile while doubling down on the innovation we bring to consumers at every touch point of our brands. As we crystallized our vision, which we actually named the Acceleration Program, we could have never predicted the ways the external environment would change with the onset of the COVID-19 pandemic. Although this profoundly altered the world around us, it reaffirmed our strategic direction. And with consistent execution, we emerged a stronger company.

Through an unwavering focus on the consumer, we acquired 15 million new customers in North America alone over the last 24 months, including approximately 7.7 million new customers in fiscal '22. Importantly, we have seen these new customers transact at higher AURs and they have returned to the brands with higher frequency. At the same time, we've increased retention rates and continued to reactivate lapsed customers across brands, all of which has led to more active customers engaging with our brands at higher average spend.

Next, we fueled significant growth in digital, which reached $2 billion in sales at accretive margins in fiscal '22, more than triple fiscal '19 levels. We see runway ahead to further increase our e-commerce sales, leveraging our established capabilities online. In addition, we grew AUR, highlighting the strength of our brands and the increasing traction of our product offerings through innovation and craftsmanship. This growth was also supported by a 40% to 50% reduction in SKU counts and a significant pullback in promotions as we utilize data and analytics to enhance our go-to-market strategies.

Overall, these accomplishments contributed to Tapestry reaching record annual revenue of $6.7 billion in the fiscal year. This performance underscores the power of our globally diversified business model in the face of a challenging backdrop. In the back half of our fiscal year, while our operations in China were materially impacted by COVID-related disruptions, outperformance throughout the rest of the world led by North America, drove strong top line growth.

Our results for the year were also fueled by gains across our portfolio with each brand delivering double-digit sales increases in the fiscal year. And we achieved accelerated growth versus fiscal '19 despite facing meaningful supply chain headwinds that required us to adapt to meet growing demand for our brands.

At the same time, we have transformed our business model, realizing $300 million in run rate expense savings, which helped to fund our growth initiatives, including a significant step up in brand marketing, which reached 8% of sales, doubling from fiscal '19. Overall, we drove earnings growth 35% ahead of pre-pandemic levels, and we utilized our robust free cash flow generation to return $1.9 billion to shareholders in fiscal '22 alone.

Importantly, we also made significant progress on many of our corporate responsibility commitments in fiscal year '22. We took bold actions through our newly created Tapestry Foundation, becoming a founding partner of FIT's Social Justice Center and establishing a partnership with the World Wildlife Fund to launch a pioneering leather traceability program in Brazil. In addition, we hired our first Chief Inclusion and Social Impact Officer, and we were a signatory of the Open to All's Mitigate Racial Bias in Retail Charter, underscoring our commitment to build a company that's equitable, inclusive and diverse.

Overall, we've made tremendous strides forward under our Acceleration Program. I'm confident in the foundation we've built, which positions us to continue to be agile in an ever-changing environment as we remain focused on moving at the speed of the consumer to drive sustainable growth across our brands for years to come.

Now turning to the highlights across each of our brands, starting with Coach. In fiscal year '22, we delivered 18% top line growth or an increase of 15% over fiscal '19 pre-pandemic levels, as we recruited over 4 million new

customers in North America while driving momentum with our existing customers. Importantly, we achieved this while delivering strong operating margin of 30%. This speaks to the heightened level of innovation we're bringing to consumers, underpinned by consistent execution and reinforcing Coach's significant potential ahead.

For the fourth quarter, we achieved a sales increase of 8% compared to prior year, including 14% growth in North America by advancing our strategic initiatives. First, we delivered a focused and compelling product assortment across categories. Our core families of Tabby, Willow, Rogue and Field, which have become pillars of our assortment, continued to resonate with consumers as we fuel innovation to maintain the relevance and emotional appeal.

In Rogue, we added new shapes, including a classic top handle handbag, as well as options in our seasonal platforms. For Tabby, the collection continues to outperform expectations, including our core women's offering and the family's recent expansion into men's with the soft messenger gaining momentum.

In addition to the Tabby expansion in men's, we delivered outsized gains overall in the men's category as well as across our lifestyle assortment, specifically footwear. Going forward, these will be important growth vehicles for Coach by increasing brand heat and top line momentum to drive customer recruitment, purchase frequency and overall basket size.

Touching on AUR. While we delivered an increase for the year, we saw pressure in the fourth quarter, primarily due to geographic mix headwinds. In North America, handbag AUR remained approximately 40% ahead of fiscal '19 pre-pandemic levels, consistent with the third quarter, though declined slightly versus prior year. Importantly, we remain confident in Coach's pricing power going forward and see further AUR opportunity in fiscal '23 helped in part by broad ticket increases, which began in August.

Second, we continue to infused data into our decision-making to ensure we're meeting the needs of the consumer while driving efficiencies in our go-to-market strategies. To this point, through product and concept testing as well as predictive analytics, we delivered a more focused and compelling assortment to consumers, resulting in higher sell-throughs and increased SKU productivity.

Third, we strengthened our consumer outreach to emotionally appeal to customers and drive engagement. Throughout the quarter, we utilized multilayer influencer strategies to amplify our offering and enhance our marketing campaigns, including on social platforms such as TikTok.

Overall, we've driven stronger customer metrics, including the acquisition of approximately 1 million new customers transacting in our North America channels. In fact, over the course of the acceleration program, Coach recruited over 8 million new customers, which included a higher penetration of millennial and Gen Z customers. Importantly, during this timeframe, we've continued to engage with our existing customers while increasing both overall spend per customer and purchase frequency.

Fourth, we invested in our digital business, which led to a low double-digit revenue increase in the quarter. As of fiscal year-end, e-commerce represented nearly 30% of sales for the brand, a material increase compared to the high single-digit penetration pre-pandemic.

Looking ahead to fiscal year '23, we are capitalizing on the foundational changes we've made and are advancing our agenda to drive continued growth at the brand. Specifically, we will focus on expanding our customer reach and increasing lifetime value by recruiting new customers with a particular focus on younger audiences while increasing overall purchase frequency and retention rates.

We will drive growth in our core leather goods [offering], continuing to build equity in iconic families, accelerate gains in men's and lifestyle categories, notably footwear and ready-to-wear, where we've been delivering outsized growth, invest in digital and China long-term, high-growth opportunities for the brand, and translate and infuse Coach's narrative into messaging across consumer touch points to reinforce our brand purpose.

In closing, Coach is an iconic brand with significant runway ahead as we continue to create deeper connectivity with consumers through innovative product, emotional storytelling and a purpose-led agenda that together, creates a virtuous flywheel for customer engagement. Our success over this past fiscal year, highlighted by a significant acceleration in sales at strong margins, underscores our confidence in the brand and its meaningful opportunity for long-term, sustainable growth.

Now moving to Kate Spade. The brand delivered record revenue of over $1.4 billion in the fiscal year, representing growth of 22%, while expanding operating margin. Throughout the year, our team has been laser-focused on rebuilding the brand's foundation and clarifying our purpose. We have delivered consistent results, a testament to our strong team, the solid execution of our strategic actions and the increasing traction and unique positioning of our brand. In fact, over the past year, in North America, we acquired over 3 million new customers, reactivated nearly 1.5 million lapsed customers and drove low double-digit growth in average customer spend.

Briefly touching on highlights from the fourth quarter, Kate Spade outperformed expectations on both the top and bottom line, reflecting progress against our growth strategies. First, we amplified key handbag platforms as we continue to build and innovate our product, infusing newness across the assortment.

Knott, our core family and #1 collection again fueled the quarter's performance, delivering strength across the offering, most notably the crossbody option, which was launched last quarter. In addition, fashion shapes, such as the Manhattan Tote and the recently introduced top handle [Merang] outpaced our expectations.

Novelty remains an important asset, a unique and differentiating factor for the brand that plays a key role in our storytelling culture. In fact, the newest novelty collections once again delivered strong sell-throughs at well above overall AUR. Importantly, the traction of our core, new introductions and novelty offering, coupled with a pullback in promotional activity, drove a low double-digit increase in global handbag AUR.

Second, we drove brand heat by engaging the consumer through emotional storytelling and a community-driven approach. Our Cabana capsule acted as an engagement engine as well as an opportunity to test product drops and build best practices.

To amplify the campaign, we launched a series of pop-ups in key cities, including New York, London and Kuala Lumpur. These locations evoke the color and joy that Kate Spade is known for, leading to new customer acquisition with over 50% of purchases made at the pop-ups from new customers. At the same time, our Kate Spade New York Cabana hashtag challenge on TikTok, which boasted a wide cast of influencers, well outpaced expectations, garnering 8 billion views since launch.

Third, we're utilizing data to maintain a consumer-centric approach and gain a deeper understanding of the preferences and drivers of customer purchases. For example, we've seen our mini and micro shapes drive recruitment of new customers, while fashion shapes and novelty resonate with our existing customer base. This knowledge comes into play as we develop our assortment architecture and targeted marketing campaigns.

Our focus on consumer centricity is highlighted by strong customer metrics. In North America, we drove an increase in the number of active customers, driven by reactivating lapsed customers and reengaging our existing customer base. At the same time, we recruited over 700,000 new customers to the brand in the quarter.

Fourth, we built on the strong foundation of our lifestyle positioning and delivered double-digit growth across ready-to-wear, footwear and jewelry. We're offering innovative and distinctive product in these categories, which emotionally connects consumers to our Kate Spade stories and the brand's DNA. Ultimately, these categories foster deeper connections with consumers, supporting higher lifetime value and global expansion.

And fifth, we have continued to invest in our digital business as we test innovative ways to engage with consumers online, including an expanded use of influencers. Overall, we've made significant progress building out this channel. In fact, Kate Spade's digital revenue represented 1/3 of total sales, well ahead of the brand's 20% penetration just 3 years ago.

Overall, Kate Spade is entering fiscal '23 with momentum. Our intent for this fiscal year is to connect more deeply with our community, leaning into the power of our brand to drive global growth.

To accomplish this, we will deliver a distinctive leather goods offering, capitalizing on the brand's unique positioning within the market and continue to drive higher AUR; accelerate lifestyle, focusing on jewelry, footwear and ready-to-wear; drive customer lifetime value by continuing to reactivate, engage existing customers while recruiting younger, more diverse customers; and fuel the emotional power of the Kate Spade brand and community through marketing that amplifies its unique positioning and universally relevant purpose.

Our success at Kate Spade is a direct reflection of the power of customer centricity and commitment to brand building. Through a focus on what differentiates the brand in the eyes of the consumer, including its lifestyle offering and community engagement through storytelling, we're resonating with new and existing customers, driving higher AUR and increasing our traction internationally. We are increasingly confident in the brand's opportunity to achieve $2 billion in revenue and a high-teens operating margin over our planning horizon.

Turning to Stuart Weitzman. Throughout fiscal '22, the brand maintained a focused strategy to drive growth, improving execution while remaining nimble to foster increasing consumer demand. The success of these actions resulted in double-digit sales gains for the fiscal year and a return to profitability despite managing through challenging external dynamics, notably COVID-related pressures in China.

In the fourth quarter, Stuart Weitzman continued to advance its growth strategies. First, we improved profitability as we leaned into strength in North America, which helped to offset the pressures in China. Despite headwinds in the margin-accretive China region, we delivered operating margin improvement compared to the prior year and above our forecast in the quarter.

Second, we maintained a consumer-centric strategy as we delivered a compelling and trend-right offering for our customers, leveraging data and analytics. Sandals were a key category as we capitalized on the increased consumer need for occasion wear. This included a standout performance from our iconic Nudist collection, which accounted for 5 of our top 10 styles.

At the same time, we increased product relevancy through newer introductions, which continue to see traction. In fact, our versatile Stuart pump, which has resonated for return to work, will be featured as a new family in fiscal '23, given the style's outperformance.

Our streamlined and relevant offering, coupled with lower promotional activity and the benefit of price increases, drove AUR growth of over 20% in North America. Going forward, we see continued opportunity to increase prices and drive full price selling while maintaining our positioning within the overall market.

Third, our engaging messaging helped to recruit new customers while continuing to reengage and reactivate clients. Fourth, we accelerated our wholesale partnerships and expanded the brand's footprint in key accounts across the globe.

Fifth, and finally, we continue to invest in digital, resulting in nearly 20% sales growth. For the fiscal year, digital represented over 20% of revenue, which while a significant increase from a low double-digit penetration pre-pandemic, highlights the significant opportunity to continue to grow our e-commerce business.

Looking ahead to fiscal '23, Stuart Weitzman's focus is to fuel continued momentum through innovation across all customer touch points with the brand. Specifically, we will spark desire with high emotion product, leaning into our authority on occasion wear and building on our casual foundation; drive brand awareness through impactful marketing campaigns; accelerate China while continuing to grow North America; increased digital revenue by continuing the online experience; and further improve profitability through a focus on high-margin growth opportunities as well as increased store productivity.

Overall, we believe these are the right strategic priorities to build brand awareness, grow market share and position the brand for continued profitable growth.

In closing, our results underscore the power of our brand, the strength of our teams and the success of our strategic actions. In addition, this performance highlights the attractive and durable nature of our categories, which have proven resilient over time, given both the emotional and functional needs they fulfill for consumers.

As we embark on a new fiscal year, the environment remains challenging and continues to rapidly evolve. However, the foundation we've built positions us to be nimble and responsive to change, balancing near-term headwinds with our long-term ambition.

Importantly, we see significant runway ahead as we harness our unique combination of authentic brands amplified by an agile and data-rich operating model. This has supported our significant acceleration over the last 3 years and is key to our ongoing success as we focus on powering our iconic brands to move with the speed of the consumer.

Overall, we are confident in our ability to drive long-term, sustainable growth and look forward to sharing the details of our financial and strategic road map at our Investor Day in September.

With that, I'll turn it over to Scott, who will discuss our financial results, capital priorities and fiscal '23 outlook. Scott?

SCOTT A. ROE, CFO & COO, TAPESTRY, INC.: Thanks, Joanne, and good morning, everyone. Looking back at fiscal year '22, we delivered strong results in the face of a volatile backdrop as we focused on the factors within our control. We have fundamentally transformed the company, creating a solid foundation that enables investment in high-return initiatives to fuel a sustainable top and bottom line growth.

This year, we delivered a record $6.7 billion in revenue; grew earnings per share 20% against last year and 35% versus pre-pandemic levels; and we returned $1.9 billion to shareholders, demonstrating our strong cash flow generation, confidence in the future and our commitment to enhancing value for all stakeholders.

Turning to the fourth quarter. Our results capped a strong year. Revenue rose 9% in constant currency or 7% on a reported basis. By region, North America again drove the results in the quarter, delivering a sales increase of 12%. Revenue in Greater China was pressured as anticipated due to headwinds associated with the pandemic, including lockdowns in major cities. As such, sales declined 32% versus last year due entirely to the pullback in store traffic as digital trends in the region rose 10% compared to the prior year.

Importantly, overall trends in Greater China improved modestly throughout the quarter and into fiscal '23. In Japan, on a year-over-year basis, sales trends accelerated meaningfully compared to the prior quarter, increasing over 25% on a constant currency basis or approximately 10% on a nominal basis.

For Europe, sales rose approximately 65% against last year with strength in both stores and online. While 1-year trends in Japan and Europe have improved significantly due to the anniversary of last year's pandemic-related headwinds as well as strong traction with domestic consumers, revenue in both regions remained below fiscal '19 pre-pandemic levels.

Across the balance of Asia, trends again accelerated sequentially on a 1-year basis, rising nearly 60%, driven by Malaysia and Singapore. By channel, sales in the margin-accretive digital channel rose high single digits in the quarter, while stores and wholesale saw continued growth.

Moving down the P&L, as expected, gross margin declined in the quarter given the incremental freight expense of $36 million, representing approximately 215 basis points of pressure as well as unfavorable geographic mix from the lower penetration of high-margin China business. That said, performance of our underlying business remains strong, and we continue to utilize data to better understand and meet the needs of our consumers while simultaneously lowering overall promotional activity.

SG&A was slightly above the prior year and better than our expectations. Even excluding the anniversary of a $25 million contribution towards the endowment of the Tapestry Foundation last year, we improved our SG&A rate, reflecting leverage across the expense base. Taken together, operating income was largely in line with our

expectations and 7% above last year. Earnings per diluted share for the quarter was $0.78, 20% ahead of last year and nearly 30% above FY '19 pre-pandemic levels.

So now turning to our balance sheet and cash flows. We ended the quarter in a strong position with $953 million in cash and investments and total borrowings of $1.69 billion. There were no borrowings outstanding under our $1.25 billion revolver.

Free cash flow for the fiscal year was an inflow of $759 million, including CapEx and implementation costs related to cloud computing of $162 million. CapEx for the year came in favorable to our expectations and included a timing shift of approximately $35 million into FY '23 due to shifts in projects mostly in Asia.

Inventory was up 35% at year-end, including an increase in in-transits of over 50% impacted by longer lead times. Overall, we're pleased with the makeup of our current inventory, which is highly penetrated in core styles. We expect inventory to end fiscal '23 up single digits versus the prior year.

Moving to our capital allocation priorities. In fiscal '22, we returned approximately $1.9 billion to shareholders. That was led by $1.6 billion in share repurchases, which is over $1 billion ahead of our original guidance for $500 million. The incremental buyback was supported by our significant free cash flow generation as well as our strong liquidity position as we emerge from the acute pressures of the COVID-19 pandemic in fiscal '21 with a more conservative cash position.

Therefore, the momentum we drove in our business and our confidence in the future allowed us to return to more normalized cash balances by the end of fiscal '22. In addition, we returned $264 million to shareholders through our dividend program.

Now looking forward, our capital allocation priorities remain unchanged. First, we're investing in the business to drive long-term, profitable growth; and second, we're returning capital to shareholders through dividends and share repurchases. Therefore, in fiscal 2023, we're planning approximately $1 billion in shareholder returns, primarily through share repurchases of $700 million under our existing $1.5 billion authorization.

In addition, our Board of Directors approved a 20% increase in our quarterly dividend, bringing our anticipated annual dividend rate to $1.20 per share. We remain committed to increasing our dividend over time at a rate faster than earnings growth.

Now moving to our outlook for fiscal 2023. We're entering '23 with a number of tailwinds. We operate in high-margin categories, which have proven to be durable and resilient. We have strength and pricing power at each of our brands, underscored by the gains we've made throughout the Acceleration Program, and margins will benefit from a reduction in incremental levels of air freight versus the prior year.

That said, our eyes are wide open, and we're not immune to headwinds that exist in our space: the appreciation of the U.S. dollar; ongoing COVID-related disruption in China; soft consumer sentiment compared to historical averages in the U.S.; and ongoing cost inflation and supply chain disruptions. In times like these, we're leveraging our established capabilities and leaning into our competitive advantages while investing in our brands to drive growth over the long term.

For the fiscal year, we expect constant currency revenue growth of 6% to 7%. On a reported basis, we anticipate revenue in the area of $6.9 billion, which represents growth of 3% to 4% and includes roughly 300 basis points of FX headwinds from the significant appreciation of the U.S. dollar.

Our guidance assumes balanced growth with all brands and channels contributing to constant currency top line gains for the year. By region at constant currency, this contemplates low to mid-single-digit growth throughout the year in North America and a gradual recovery in Greater China resulting in growth for the fiscal year as well as double-digit gains in Japan and Europe.

In addition, we anticipate a year-over-year operating margin decline in the area of 50 basis points, due entirely to FX headwinds of roughly 100 basis points. This contemplates gross margin relatively in line with the prior year, reflecting the benefit of moderating freight costs as well as AUR increases across all brands. We expect these tailwinds to be partially offset by the previously anticipated rising input costs for materials as well as the negative impact of FX. On SG&A, we anticipate modest deleverage for the year, reflecting continued investments in growth drivers, including digital and the planned 2023 opening of our new fulfillment center in Las Vegas.

Moving to below line items. Net interest expense for the year is anticipated to be approximately $35 million, a significant decline versus fiscal '22, reflecting the benefit of our recently executed cross-currency swap arrangements. Tax rate is expected to be approximately 21%. This represents an increase against last year, primarily due to the anticipated geographic mix of earnings.

Weighted average diluted share count is expected to be in the area of 242 million shares. This reflects approximately $700 million in share repurchases expected for the fiscal year as noted. So taken together, we expect EPS of $3.80 to $3.90, representing double-digit growth compared to the prior year.

Finally, CapEx and cloud computing costs are forecasted to be in the area of $325 million, including the previously mentioned $35 million shift from fiscal '22. We anticipate approximately half of the spend to be related to new stores and renovations, primarily in China, with the balance dedicated to our ongoing digital and IT initiatives and investments related to our new fulfillment center in Las Vegas.

Given the volatile environment and last year's atypical comparisons, we again expect significant variability by quarter. Specifically, we expect revenue and earnings growth versus prior year to be back half weighted, helped by the sequential improvement planned in China as we move throughout the year. In addition, we will anniversary the substantial incremental headwinds from freight beginning in the second fiscal quarter of the year, providing a tailwind to margin.

For the first quarter, we expect revenue to increase mid-single digits in constant currency, which included a decline of approximately 15% projected in Greater China. On a reported basis, we anticipate global sales to increase slightly, including a negative impact of approximately 350 basis points from FX with EPS in the area of $0.75.

In closing, we delivered strong results in fiscal '22 with 18% top line growth driving record annual sales. EPS increased 20% versus prior year and 35% over pre-pandemic levels. At the same time, we returned $1.9 billion to shareholders. This is a testament to the resilience of the categories where we play, the strength of our brands, the benefits of our transformed globally diversified business model and our talented teams around the world who continue to drive our strong performance.

As we look forward, we remain confident in our trajectory and disciplined in our approach to driving long-term sustainable growth and total shareholder return.

And now I'll open it up for your questions.

Questions and Answers

OPERATOR: (Operator Instructions) We'll take our first question from Bob Drbul of Guggenheim Securities.

ROBERT SCOTT DRBUL, SENIOR MD, GUGGENHEIM SECURITIES, LLC, RESEARCH DIVISION: I guess, Joanne, I was wondering, when you look at the last couple of years, as you guys think about FY '23, the environment is clearly challenging. Can you just talk about the confidence that you guys have that you can deliver another strong year for shareholders?

JOANNE C. CREVOISERAT: I would say that we're confident in our ability to connect with the consumer. Over the last 2 years, we've gained 15 million new customers in North America alone. And we just -- as you pointed out, we just delivered a great year.

We posted record revenue levels, double-digit growth at each of our brands. And those results last year and over the past 2 years have been delivered in a very difficult retirement. We saw top and bottom line growth over that period, and we're up double digits to pre-pandemic levels. And that really speaks to the success of our Acceleration Program. We've built a very strong foundation, and we see significant runway ahead.

Given the macro backdrop, as you mentioned, we believe that our outlook is both prudent and realistic. We expect constant currency 6% to 7% growth for the year. And some of the drivers of our confidence, it starts with our team.

I believe we have the best team in the business. Our team has proven to have agility, and we've been responsive to all of the changes that we've seen in the backdrop. Our brands are strong and getting stronger. And over the last 3 years, we've really pivoted the company with -- to have a real focus on brand building and brand building capabilities, and we're investing behind that and in the future of our brands.

We play in attractive categories. The categories that we serve our customers have proven to be resilient over time and durable. And I think the success of our transformation is really underpinned by our laser focus on the customer. We're staying closer and closer to our customers and executing behind that. And not only are we calling for growth in this fiscal year, but we see a tremendous amount of runway ahead across each of our brands, and we're looking forward to sharing more of those details at our Investor Day coming up next month.

OPERATOR: (Operator Instructions) We'll move next to Ike Boruchow of Wells Fargo.

IRWIN BERNARD BORUCHOW, MD AND SENIOR SPECIALTY RETAIL ANALYST, WELLS FARGO SECURITIES, LLC, RESEARCH DIVISION: Scott, you gave some additional color to the fiscal year guide, but I just wanted to follow up. Is there more you can provide us on the shape of the year? There's a lot of variability first half, back half with freight in China, et cetera. So any other help on the shape would be helpful. And then on GSP, I see that that's not included in the guide, but if that does go through, can you just remind us the EPS benefit on an annualized benefit that you guys would see?

SCOTT A. ROE: Sure, Ike. Thanks for the question. So on the first part, maybe a little more unpacking on the shape of the year by quarter. So first of all, in North America, Joanne's comments, we do see some moderation in our growth. We talked about low to mid-single-digit growth. But importantly, that's off a base of growing last year, 28%, almost 30%. And on a pre-pandemic stack, more than 22%. So our business in North America is strong. It remains strong. And we expect that to be consistent throughout each of the quarters as we go through the 4 quarters of the year.

Next, I'll address the rest of the world excluding China. And again, very strong year-on-year growth. Not quite as -- we're recovering there, not quite as strong on the 2-year stack. But versus last year, where we saw severe COVID impacts, Japan, rest of Asia, we're seeing very strong double-digit growth, more than 20% in most regions, and we expect that to continue throughout the year.

The one that's a little different is China, as mentioned in the prepared remarks. Just some perspective there, last quarter, we were down about 32%. That's a little better than we had guided. We guided down 35%. And importantly, as we exited the year and entered this year, we see the trends improving and continue to improve. So we've really just taken the trend line that we see and projected that through the balance of the year.

So by Q3, we inflected the growth. And for the full year, we see a single-digit growth in China. So that regional difference by year really accounts for a lot of the progression. It's really a consistency in the trends that we see. It's not a big change in trend, it's just the mathematics of how those different regions come together.

And then one -- in addition to the revenue cadence by quarter, we should also talk about some of the profitability drivers. And the biggest one is freight. So you may recall, we've talked about freight last year being elevated for 2 reasons. Ocean rate's up as well as air freight. And we're essentially out of the air freight business, but it takes a while for that rabbit to work through the snake, right? And as that inventory -- or the freight is attached to that inventory, we're going to see still some negative impact year-on-year in Q1 because we don't start anniversarying the big air freight until Q2 and beyond.

So in putting some numbers on that. In Q1, we still expect a headwind from freight somewhere around 150 basis points on the negative. That inflects in Q2 and beyond. And for the year, we see about 80 basis points of favorability in freight. And importantly, from Q2 through Q4, so Qs 2, 3 and 4, that's going to be about 140 basis points favorability to last year, and that gets you to that ongoing rate of about half of what we saw last year coming back to us as a tailwind.

And then the last point that creates just a little noise is FX. So FX, we mentioned in the prepared remarks, about 300 basis points impact on top line, about 100 basis points on bottom line. That's a little more acute in the first quarter, about 350 basis points as we start to lap some of the movements in the in the USD as we move through the balance of the year. So hopefully, that gives you a little bit of context on the shape.

Second part of your question was GSP. As you noted, we did not reflect any assumption and changes in the law around GSP. It's about $40 million in the annual duties paid because we don't have the GSP regime in place. And if it should be retroactive, which in all recent past, it always has been, that would be about another $50 million. So $90 million in total, assuming that it's passed and assuming that it's retroactive. So a significant impact, it's $0.30-plus or so.

OPERATOR: Our next question comes from Lorraine Hutchinson of Bank of America.

LORRAINE CORRINE MAIKIS HUTCHINSON, MD IN EQUITY RESEARCH, BOFA SECURITIES, RESEARCH DIVISION: Can you give us your thoughts on how of the store fleet, and how you think about the footprint for each brand now that e-commerce is such a bigger part of the business?

JOANNE C. CREVOISERAT: Yes. We feel really good about our store fleet and the health of our store fleet. We had -- over the last 3 years, had a focus on improving the productivity and profitability of our store fleet and also understanding and making sure that we're delivering the right experience for our consumers in that physical touch point.

And we believe stores are still important to the consumer, and it represents, as I said, an important touch point. But with our focus on the profitability, even as we've come through the pandemic and had traffic pressures, our store fleet is more profitable than it was pre-pandemic level today, even today. So we feel good about where we're positioned, and we see opportunities to continue to work to improve the experience we're delivering to consumers in that physical touch point as really an important part of the consumer shopping journey.

Importantly, to your point, we've driven an incredible growth in our digital business. We've reached $2 billion in that business, more than triple where we were pre-pandemic. And it's important because we've taken a focus shifting from a specifically channel focus to focusing on the consumer, and we want to be where the consumer is in terms of how to engage the consumer with our brands.

And we've, again, lots of traction in digital. It's a $2 billion business. It comes with accretive margins versus the brick-and-mortar channel. So for us, seeing that continued growth is a good thing and a good outcome. But at the same time, we're improving profitability of our store fleet. And altogether, we're acquiring new customers across these channels, which is really healthy for our brands, including an increasing number of younger consumers.

So that's how we're thinking about stores. We'll continue to test and learn in the omnichannel capabilities for our store and make sure we're delivering the right experience for our consumers there.

OPERATOR: Our next question comes from Michael Binetti of Credit Suisse.

MICHAEL CHARLES BINETTI, RESEARCH ANALYST, CRéDIT SUISSE AG, RESEARCH DIVISION: I think your -- on the AUR comment, Joanne, did I hear you correctly that North America handbag AUR was negative year-over-year in the quarter? And I know you said global, I'm assuming a lot of that was from China mix. I'm curious on North America. And I think you referenced some ticket increases in August. Maybe the size there and what -- whether the 1Q plan bakes in a return to positive AUR for the Coach brand in North America.

JOANNE C. CREVOISERAT: Yes, I'll kick it off by saying -- and then I'll toss it to Todd for some color on Coach. AUR, it continues to be -- we continue to see pricing power across our brands. And for the quarter overall, we saw AUR growth.

In the Coach brand, in the fourth quarter, though we parse it out, Coach has been successful driving AUR growth for 3 years. And a lot of that is due to our focus on the consumer and delivering value and really leveraging data and analytics from our -- in our platform, but also delivering the innovation that the customers value.

And again, 3 years of a strong track record in the fourth quarter, the Coach brand in North America was down slightly, but still 40% above pre-pandemic levels. So that gives you, I think, an understanding of the pace of change that we've made in the Coach brand.

But that -- we still see continued opportunity for growth ahead, and I'll let Todd touch on that. In our other brands, the Kate and Stuart, we're much earlier on that journey and continue to drive strong AUR growth and see runway ahead in those brands as well. So bringing the power of our data-rich platform and our consumer centricity forward, it has had traction, and we see that going forward. But Todd, I'll let you provide some color on Coach specifically.

TODD KAHN, CEO & BRAND PRESIDENT OF COACH, TAPESTRY, INC.: Thank you, Joanne. As Joanne indicated, we're coming off some amazing numbers, 40% above pre-pandemic in North America. And what we had said to you before was we had always planned on ticket increases this August and throughout the year. And generally speaking, it's about 6%, sometimes a little higher, sometimes in that range. And we feel very good about that.

We feel good about that because we've not seen any resistance from our consumer, and they really appreciate the coats that Coach offers that are unique, the value and the innovation. And we anticipate seeing a return to AUR growth even in North America handbags in the first quarter and throughout the year.

OPERATOR: Our next question is from Adrienne Yih of Barclays.

ADRIENNE EUGENIA YIH-TENNANT, MD, SENIOR ECOMMERCE & BRAND RETAILING ANALYST, BARCLAYS BANK PLC, RESEARCH DIVISION: Nice end to a fantastic year. Joanne, I wanted to go back to the comment on the 40% to 50% SKU reduction. What categories -- or did you just kind of tighten up for the AUR, the target AUR? Did you take out certain categories? So any more color on that piece of it.

And then, Todd, how much of the product, the production/design process is based on predictive analytics? And how do you balance sort of your creative force of the team versus the more analytical nature of kind of data analytics?

JOANNE C. CREVOISERAT: Yes. Thanks, Adrienne. I'll kick it off with our AUR and some of the data and analytics approach to how we thought about SKU reduction. And your point on understanding the assortment, we leveraged data and analytics to really help drive our SKU reduction efforts.

We wanted to make sure that we did have the right assortment architecture and we cut a lot of the tail of the unproductive SKUs. But importantly, we leveraged analytics and market research to understand the consumer across the landscape and make sure that we had the right products to deliver against an understanding, a deeper understanding of the customer.

So as we developed our assortment architecture, understanding who the consumer is, who the target consumer is and where we wanted to place our bets. And it's been an important and a huge win for us as we've come through a pretty volatile environment to have that focused assortment that has -- each SKU has a purpose, and we're evaluating which SKUs are attracting new customers, what are the entry points for our brands, where are we seeing customers move up in AUR and delivering that value that they recognize.

It's been a tremendous help to have more focused assortment as we navigate a lot of the supply and demand changes around the world. And it's been a tremendous help in terms of communicating to the consumer what's important. So with all of the changes that have happened over the last 2 years, we're better at identifying the SKUs.

We're better at allocating those items, that assortment across the world. We're better at allocating our inventory behind those, and we're better at messaging our consumers behind the reduced SKU count. So a lot of wins on that score.

TODD KAHN: What I can add is our designers are not going to be replaced by AI any time soon. So what we've said often in the past is we are at our best when we blend magic and logic. And today, what that means is all the things that Joanne mentioned. But in addition, it's informing the creative process, it's informing design. We're having much better feedback loops earlier.

And again, I want to make sure we continue to be innovative and creative, and that is not going to be something that we're outsourcing to computers. Stuart Vevers and his team really come up with incredible ideas and focus. And their goal, their muse is this younger consumer, this global consumer that cares about values that we infuse in the brand.

So again, it's an informed creative process. We're at our best when we do this. We're using the Tapestry platform and the data to help us do this in a really authentic way, and you're seeing it in the product.

OPERATOR: Our next question is from Mark Altschwager of Baird.

MARK R. ALTSCHWAGER, SENIOR RESEARCH ANALYST, ROBERT W. BAIRD & CO. INCORPORATED, RESEARCH DIVISION: It's been great to see the continued progress at Kate. Can you give us some updated perspective on the path to $2 billion? And how are you thinking about growth by geography? And at what point does China become a bigger part of the story again?

JOANNE C. CREVOISERAT: Well, we see, Mark, the opportunity to achieve $2 billion. We're increasingly confident in that as the team has really delivered and the brand is really performing, both on top and bottom line. And we see that traction with our existing customers. That has been our focus, right, to get the brand steady and growing in our core markets of North America and Japan. And we see tremendous runway and opportunity ahead to get to that $2 billion with growth in our core markets.

We also, though, to your point, see opportunity to expand internationally. We've driven strong growth. Our business is small in both China and Europe. Europe has been performing quite well. We see opportunities to expand there. And over time, also impact the China market. So that is an opportunity.

The $2 billion is not contingent upon a big step into China. We see runway in our core markets in addition to China, which is, right now, it represents a lot of white space for the brand to continue to grow beyond $2 billion.

OPERATOR: Our next question is from Oliver Chen of Cowen.

OLIVER CHEN, MD & SENIOR EQUITY RESEARCH ANALYST, COWEN AND COMPANY, LLC, RESEARCH DIVISION: Joanne and Scott, our survey data at Cowen is showing some pressure on the higher-end customer as well. Just would love your thoughts on the strategy for the average unit retail increases at the Coach brand in the fourth year of doing this, just the nature of what's achievable yet still offering clear value and innovation.

And Joanne, you mentioned younger customer in your prepared remarks as well as opportunity for continued brand building. Could you be more specific about what you mean there and where you see the evolution of the innovation going?

JOANNE C. CREVOISERAT: Yes. Why don't I toss it to Todd to talk about the Coach brand, and then I'll follow it up with our young consumer.

TODD KAHN: Thank you. We feel really good about where we are in AUR and particularly the place you focused on, which is the higher end. Two quick data points. First of all, in retail, we saw AUR handbag growth even in the fourth quarter. And what that shows is the dramatic white space that exists today between Coach and the traditional European luxury brands. And I think what you see with Rogue and some of our more elevated products, the consumer is recognizing the value there and there's a lot of opportunity to continue to grow there.

And so I see us further increase our AURs throughout the year, both in North America and globally. And we're going to see that in Japan, in China, coupled with innovation, I feel very good, particularly about us capturing more of that white space.

JOANNE C. CREVOISERAT: And let me just follow up with -- to answer the second part of your question, Oliver, on brand building, we have spent the last 3 years really pivoting the company to get focused on how we continue to invest in our brands. And as we've done that, we've focused on acquiring new customers, reactivating the customers, lapsed customers and continuing to drive higher customer lifetime value. And that focus on the customer is part of our brand building story.

We are trying to acquire more customers and succeeding, 15 million new customers in the last 2 years alone. And we are seeing an increasing number of younger consumers. And we're doing that with capabilities that we've developed in marketing and also with data and how we're positioning our assortment, so understanding that consumer, getting closer to that consumer and delivering product and experiences that they value. And again, we're seeing traction. We're showing up in the places where they are, particularly on digital channels. And we're showing up not only for the transaction, but engaging consumers as they're on their journey, the customer journey and discovery.

So part of our investments, and we talked about how we've significantly changed our investments to be behind that brand building and in digital, moving our marketing spend from 4% of sales to 8% of sales is meaningful. And we have the capabilities to continue to measure the effectiveness of the investments we're making and ensuring that we're getting the outcomes that we want. And you can see those results again in the customer acquisition over the last 2 years, and we expect that to continue.

OPERATOR: Our next question is from Brooke Roach of Goldman Sachs.

BROOKE SILER ROACH, RESEARCH ANALYST, GOLDMAN SACHS GROUP, INC., RESEARCH DIVISION: Joanne, I'd love to hear your outlook for growth for the accessories and handbag category into fiscal '23 for both units and AUR. Where do you see the largest opportunity for Coach brand to take share in the North American handbag and accessories market this year?

JOANNE C. CREVOISERAT: Yes. We are fortunate to play in a category that has historically had very -- proven very resilient and had durable growth over years. We've seen pre-pandemic, the category grow in the mid- to high single-digit range very consistently. And even through the pandemic, we saw consumers engaging with the category and coming out strong as we've recovered from the pandemic. But going forward, we expect the category to continue to grow in that mid- to high single-digit level.

And from the Coach brand, I give Todd and the team at Coach tremendous credit. They have really infused life and energy into that brand. We're acquiring new customers, we're driving innovation and really managing the business quite well. And you can see that in the customer acquisition that we're seeing at the Coach brand, we still have tremendous runway ahead for Coach. The category, we see growing, and we think Coach is very well positioned to continue to grow with the category at very strong margins.

TODD KAHN: Yes. I think the only thing I can point you to is it was very interesting, recently, the business of fashion did a very deep dive in the handbag category. And with unaided awareness, they were asked, consumers who were engaged in the category and anticipated buying a brand, what brand would they buy? And we were very pleased to see that Coach was the #1 brand in the U.S. on an unaided awareness by consumers who have the intention to buy.

Even -- what was also very interesting was on high net worth individuals, individuals who have over 1.5 million investable assets, Coach was #5 in the U.S. So that bodes very well and shows that we are cutting through in our messaging on values. And I think you're going to see us, and you're going to hear us talk quite a bit about it at the upcoming Investor Day, how we're going to chart our future and take us into the next meaningful growth period for Coach.

OPERATOR: Our next question is from Dana Telsey of Telsey Advisory Group.

DANA LAUREN TELSEY, CEO & CHIEF RESEARCH OFFICER, TELSEY ADVISORY GROUP LLC: Can you talk a little bit for each of the brands where you are on the journey of price increases? And does it at all differ in terms of how you're pricing for some of your exclusive or limited edition products?

JOANNE C. CREVOISERAT: Dana, first, I'll start by saying we occupy an incredible position in the market, and we represent tremendous value for the quality and the innovation that we're delivering to consumers, and consumers are recognizing that. We have been seeing AUR growth consistently at Coach for 3 years. And consumers are recognizing the value that we're delivering in the marketplace.

Where we are in the journey, we still see runway ahead across all 3 brands to drive AUR. We see pricing power across our brands, again, with customers recognizing that value. While Coach is further along on this journey, again, and as Todd just mentioned, we see runway ahead to drive more price increases, more than offsetting inflationary input cost pressures as we move forward and as we deliver -- continue to deliver great value in the market.

And in the context of the market, we've seen the Pinnacle luxury players move price up pretty substantially over the last 3 years. And that creates that white space for all of our brands to position our -- and continue to position AUR higher.

And again, at Kate Spade and at Stuart Weitzman, continuing to see strong AUR growth in the last quarter over the last year, earlier on the journey, so much more runway ahead in those brands as well.

OPERATOR: Thank you. That concludes our question-and-answer session this morning. I will now turn the call over to Joanne for some concluding remarks.

JOANNE C. CREVOISERAT: Thanks, operator. I want to close by thanking our teams around the world for their passion and commitment. They drove these standout results that we delivered. We delivered record annual revenue this year with double-digit growth at each brand and our digital business reaching $2 billion, along with earnings 20% above last year. So a standout performance, really clearly demonstrating the strength of our brands and the power of our transformation, which positions us well for the future.

We have significant long-term runway. And through a continued focus on the customer and commitment to brand building, I'm confident in our ability to drive sustainable growth going forward. I'm looking forward to sharing more details on our long-term road map at our Investor Day next month, and I hope to see you all there. Thank you.

OPERATOR: This does conclude the Tapestry earnings call. We thank you for your participation. You may now disconnect your lines. And everyone, have a great day.

Load-Date: August 20, 2022
